LIBRARY
SUPREME COURT, U. S.

No. 71

Office - Supreme Court, U.S.
FILED
JUN 27 1958
JOHN T. FEY, Clerk

# In the Supreme Court of the United States

October Term, 1957

---

A. L. WASSON and Wife, MATTIE PALLMEYER WASSON, PETITIONERS

*v.*

UNITED STATES OF AMERICA

---

***On Petition for a Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit***

---

## BRIEF FOR THE UNITED STATES IN OPPOSITION

---

J. LEE RANKIN,
*Solicitor General,*

CHARLES K. RICE,
*Assistant Attorney General,*

ROBERT N. ANDERSON,
DAVIS W. MORTON, JR.
*Attorneys,*
*Department of Justice,*
*Washington 25, D. C.*

# INDEX


| | Page |
|---|---|
| Opinions below | 1 |
| Jurisdiction | 1 |
| Questions presented | 2 |
| Statute and regulations involved | 3 |
| Statement | 3 |
| Argument | 6 |
| Conclusion | 11 |
| Appendix | 12 |


## CITATIONS

Cases:


| | |
|---|---|
| *Hughes* v. *Commissioner*, 15 B.T.A. 215 | 9 |
| *Hughes* v. *Commissioner*, 38 F. 2d 755 | 8 |
| *Real Estate Title Co.* v. *United States*, 309 U.S. 13 | 9 |
| *United States* v. *Felt & Tarrant Co.*, 283 U. S. 269 | 9 |
| *Weinstein* v. *Commissioner*, 29 T.C. 142 | 10 |


Statutes:


| | |
|---|---|
| Internal Revenue Code of 1939: | |
| Sec. 23(e) (26 U.S.C. 23(e)) | 3, 12 |
| Sec. 23(o) (26 U.S.C. 23(o)) | 3, 8, 12 |
| Sec. 23(s) (26 U.S.C. 23(s)) | 3, 13 |
| Sec. 41 (26 U.S.C. 41) | 3, 7, 13 |
| Sec. 117(b) (26 U.S.C. 117(b)) | 3, 10, 11, 13 |
| Sec. 117(e) (26 U.S.C. 117(c)) | 3, 10, 13 |
| Sec. 122(a) (26 U.S.C. 122(a)) | 3, 14-15 |
| Sec. 122(d) (26 U.S.C. 122(d)) | 3, 5, 10, 11, 15 |
| Revenue Act of 1921, 42 Stat. 227, Sec. 204(a) | 9 |


Miscellaneous:


| | |
|---|---|
| Treasury Regulations 111: | |
| Sec. 29.41-1 | 3, 15 |
| Sec. 29.122-3 | 3, 16 |
| Sec. 29.122-4 | 3, 16 |

# In the Supreme Court of the United States

October Term, 1957

---

No. 1031

A. L. WASSON and Wife, MATTIE PALLMEYER WASSON, PETITIONERS

*v.*

UNITED STATES OF AMERICA

---

***On Petition for a Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit***

---

## BRIEF FOR THE UNITED STATES IN OPPOSITION

---

### OPINIONS BELOW

The findings of fact and conclusions of law of the District Court (Pet. 37-39; R. 209-216) are not reported. The opinion of the Court of Appeals (Pet. 26-36) is reported at 250 F. 2d 826.

### JURISDICTION

The judgment of the Court of Appeals was entered on January 7, 1958. The taxpayers' petition for rehearing was filed on January 15, 1958, and denied

on February 28, 1958. The petition for a writ of certiorari was filed on May 28, 1958. The jurisdiction of this Court is invoked under 28 U.S.C. 1254.

## QUESTIONS PRESENTED

Whether under Section 122 of the Internal Revenue Code of 1939, as amended, the taxpayer[1] is entitled to all or any of five claimed adjustments pertaining to the conversion of a 1951 net operating loss into a 1950 net operating loss carry-back deduction:

(1) An additional deduction on the taxpayer's individual 1951 return for sheep purchases, incident to an unrecorded transfer of 508 sheep by Wasson and Carter, a ranching partnership;

(2) An additional deduction on the taxpayer's 1951 return with respect to a wool inventory carried by Wasson and Carter;

(3) An addition to the taxpayer's 1951 net operating loss, by reason of contributions claimed on his individual return for that year;

(4) An alleged right to submit proof of cost depletion not specified in the claim for refund, the Commissioner having made an adjustment under Section 122 (d) (1) of the Internal Revenue Code of 1939 for claimed percentage depletion; and

(5) An alleged Section 122(d)(4) computation error pertinent to the determination of the net operating loss carry-back deduction for the taxable year 1950, based on a claimed failure by the Commis-

---

[1] The term taxpayer refers to A. L. Wasson.

sioner to take into account, under Section 117(e) of the 1939 Code, a net capital loss of $28,756.79, which had been carried over from the preceding 1949 taxable year.

## STATUTE AND REGULATIONS INVOLVED

Sections 23(e), (o), and (s), 41, 117(b) and (e), and 122(a) and (d) of the Internal Revenue Code of 1939 and Sections 29.41-1, 29.122-3(a), and 29.122-4(a), of Treasury Regulations 111 are set forth in the Appendix, *infra*, pp. 12-17.

## STATEMENT

The pertinent facts, as found by the District Court (Pet. 37-38; R. 210-213) and adopted, insofar as here applicable, by the Court of Appeals (Pet. 26-36) are as follows:

This action was brought to recover income taxes paid for the calendar year 1950. On March 15, 1951, A. L. Wasson filed a joint income tax return for the taxable year 1950 for himself and Mrs. Mattie E. Wasson, deceased. This return was amended on September 15, 1953, to show a net income of $85,951.18 and an overpayment of tax in the amount of $27,499.96, based in large measure on a claimed net operating loss carry-back deduction from the subsequent year, 1951, in the amount of $94,820.15. For the year 1951, A. L. Wasson originally filed a separate return, which was later amended, on September 15, 1953, to show a net operating loss of $94,820.15. The amended 1951

return included losses attributable to certain partnership interests, including Wasson and Carter, a ranching partnership in which taxpayer had the the principal interest. (R. 210-211.)

The taxpayer's books and records, including those of Wasson and Carter, did not reflect a definite method nor did they clearly reflect income. Based on evidence submitted by both parties, the taxpayers were on a cash receipts and disbursement basis. (Pet.-37; R. 211.)

A. L. Wasson's books for 1951 showed losses (largely sheep and cattle losses) which he contended were his separate losses and should be used in computing his net operating loss carry-back from 1951 to 1950 (R. 211)[2].

In 1951, there was an unrecorded transfer from the partnership of Wasson and Carter to A. L. Wasson of 508 head of sheep. This resulted in an understatement of sales of the partnership in the sum of $5,924, which had no effect on the personal return of the taxpayer since these sheep would have been included in his closing inventory, thereby reducing the number of sheep sold or lost. (R. 212.)

For the taxable year 1949, A. L. Wasson and his then wife had a net capital loss in the amount of $29,756.79, which, when reduced by the $1,000 capital loss allowable for the year 1949, left a capital loss to be carried forward to the year 1950 in the amount of $28,756.79. For the taxable year 1950, the taxpayer had a long-term capital gain of $48,008.43

[2] This contention, described as Point One in the Court of Appeals, was accepted by that court. (Pet. 26, fn. 1; 36.)

(50% of $96,016.86). Combined with the capital loss carry-forward, this produced a net capital gain for the year 1950 in the amount of $19,251.64. There was no capital loss carry-over to 1951 as the entire amount was absorbed by the 1950 capital gain. (Pet. 38; R. 213.)

On the basis of the above findings, the District Court concluded, so far as is here pertinent:

> The Commissioner has wide discretion in determining the method of accounting where the books do not reflect a definite method or clearly reflect income. The use of inventories by the taxpayer is not conclusive on this question. The Commissioner's finding that the taxpayer was on a cash receipts and disbursement basis is upheld. The accrued expenses were properly disallowed. (Pet. 38; R. 214.)
>
> On the issue of understatement of sheep sales of the partnership of Wasson and Carter, it has been found as a fact that there was an unrecorded transfer from the partnership to the taxpayer of 508 head of sheep. This resulted in an understatement of sales of the partnership with no effect on the personal return of Wasson since these sheep would have been included in his closing inventory, thereby reducing the number of sheep sold or lost. (Pet. 39; R. 215.)
>
> Section 122(d)(4) of the Internal Revenue Code of 1939 does not apply to affect the capital loss carryover from 1949. (Pet. 39; R. 216.)

The Court of Appeals, while it reversed the District Court on an issue not here involved, affirmed its findings on the points raised in this Court (Pet. 36).

## ARGUMENT

This case does not warrant further review. No general or important question of federal income tax law is presented. Each issue here raised depends upon the factual context of this particular case. Moreover, there is no conflict of decisions.

1. In his contention under question 1, which concededly constitutes merely "a problem in accounting" (Pet. 9-10), the taxpayer attempts to ascribe unwarranted significance to Finding 14 (Pet. 37-38; R. 212), which approved, in effect, an adjustment of $3,924 made to Wasson and Carter's 1951 sales as a result of the unrecorded transfer of 508 sheep to taxpayer, A. L. Wasson, individually, on November 8, 1951 (R. 14). While the taxpayer does not attack this finding (Pet. 10), he does assert that there should be an additional adjustment to A. L. Wasson's 1951 net operating loss by way of a corresponding increase in purchases by the latter. As the trial court found (Pet. 38), "these sheep would have been included in his closing inventory, thereby reducing the number of sheep sold or lost." The effect of the adjustment was to increase the partnership's sales (a profit and loss item, accounting-wise) and this, in turn, resulted in a corresponding decrease in Wasson's distributive share of the firm's 1951 loss. The error of assuming that the taxpayer's books should be adjusted to reflect the cost of these sheep (Pet. 10-11) appears from the District Court's finding (Pet. 37; R. 211) that Wasson was "on a cash receipt and disbursements basis." No evidence was adduced that

Wasson made any cash outlay that could serve as the basis for the alleged "Purchase of sheep" (Pet. 11) upon which taxpayer's erroneous claim is predicated.

2. Under question 2 (Pet. 12-16), the gravamen of the taxpayer's complaint is that the courts below did not revise the Wasson and Carter partnership's system of tax accounting to make an adjustment in a 1951 item of wool inventory. However, no contention with respect to this belatedly claimed adjustment was made by taxpayer before the District Court. Moreover, Wasson and Carter was not a party to this litigation. Its 1951 operations have relevance, for present purposes, to the extent that adjustments affecting taxpayer's distributive share of its reported 1951 loss were challenged at the trial. In addition to the unrecorded sheep transfer, discussed in connection with question 1, *supra*, such adjustments included the Commissioner's disallowance of accrued taxes, rent, and interest. (Taxpayer's C.A. Br. 2; R. 18, 21, 64.) In disallowing such accrued expenses, the revenue agent had ample justification since the partnership was not the record owner of New Mexico land on the date the accrued taxes became a lien (R. 19-20), accrued rent was not amortized over the leasehold life (R. 21), and no verification could be secured that the accrued interest was even paid (R. 64). Therefore, since no reliable tax accrual method was in effect with respect to these specific disallowances, the Commissioner was clearly empowered, under Section 41 of the 1939 Code (Appendix, *infra*), to disregard the partnership's purported accrual method of accounting to the extent

that it did not "clearly reflect the income." In this regard only was it necessary to disturb Wasson and Carter's regularly employed method of tax accounting. Clearly, as to other phases of the partnership's operations, such as the wool inventory which was not in issue, no duty devolved on the Commissioner to make adjustments. Accordingly, the District Court was correct in finding (Pet. 37) that, whereas "taxpayers were on a cash receipt and disbursements basis", the "books and records * * * of Wasson and Carter, did not reflect a definite method nor did they clearly reflect income." This finding, adequately supported by the facts presented, authorized the exercise of the Commissioner's discretion in disallowing the claimed expenses, and in limiting the adjustments to the issues raised.

3. The taxpayer's claim (question 3 (Pet. 16-18)) to an additional 1951 net operating loss on account of contributions runs contrary to the express provisions of the 1939 Code. Section 23(o) (Appendix, *infra*), permits individuals, whether on a cash or accrual basis, to take a limited deduction (*viz.*, 15 percent of *adjusted gross income*) only for the year in which the contribution is paid. Accordingly, since taxpayer had no adjusted gross income in 1951, the loss year, no statutory basis exists for taking any contributions deduction. The alleged conflict (Pet. 16, 17-18) with *Hughes* v. *Commissioner*, 38 F. 2d 755 (C.A. 10), does not exist. The precise contributions issue, here raised, had there been considered by the Board of Tax Appeals below and decided for the Commissioner for the reasons we rely on here.

*Hughes* v. *Commissioner*, 15 B.T.A. 215, 219. In reversing the Board, on appeal, the Tenth Circuit did not address itself specifically to the contributions issue but, instead, confined its attention (p. 757) to the question of the meaning of the phrase "trade or business", as used in Section 204(a) of the Revenue Act of 1921, 42 Stat. 227, and concluded (p. 759) that income from the taxpayer's law practice, from salaries and from dividends was not embraced within the meaning of that particular statute.

4. Under question 4 (Pet. 18-21), the taxpayer reiterates a contention, raised both on appeal and on motion for rehearing, against the District Court's ruling sustaining an objection by Government counsel (R. 34) to the introduction of evidence concerning alleged cost depletion attributable to A. L. Wasson on a royalty interest of the Wasson Oil Company, a non-party partnership. This contention is plainly without merit. No claim for cost depletion was set out in the claims for refund. (R. 32-33.) Accordingly, the District Court lacked jurisdiction to consider the problem. *United States* v. *Felt & Tarrant Co.*, 283 U.S. 269; *Real Estate Title Co.* v. *United States*, 309 U.S. 13. Moreover, revenue agent Hawkins, who had been called as the taxpayer's witness, had no knowledge of any cost basis that the taxpayer A. L. Wasson might have had (R. 28), nor was he familiar with any prior revenue reports concerning the estate of A. L. Wasson's first wife, Mattie E. Wasson (R. 28-29).

5. Finally, under question 5 (Pet. 21-25), which is essentially a computation problem, the taxpayer

mistakenly attempts to claim an additional 1950 deduction of $28,756.79 (Pet. 8) on the erroneous assumption that a 1949 net capital loss in that amount[3] constituted (Pet. 3) a carry-over item under Section 117(e)[4] which, allegedly, had not been fully taken into account in making the required Section 122(d)(4) capital gains and losses adjustment[5] to 1950 income incident to computation of the applicable 1951 net operating loss carry-back deduction to that year. As authority for such claim, the taxpayer relies (Pet. 23) essentially on the recent decision in *Weinstein* v. *Commissioner*, 29 T.C. 142, 149. The holding re-

---

[3] Under Section 117(e)(1) of the 1939 Code (Appendix, *infra*), this $28,756.79 net capital loss carry-over from 1949 (Pet. 38; R. 213) had initially been applied against 1950 short and long-term capital gain in originally reporting taxpayer A. L. Wasson's tax liability for the latter year, prior to incurrence of the subsequent 1951 net operating loss, which necessitated the computation, under Section 122(d)(4) of the 1939 Code (Appendix, *infra*), of the net operating loss carry-back deduction applicable to the taxable year 1950. According to his 1950 return taxpayer A. L. Wasson had a capital gain for that year of $48,008.43 (50 percent of $96,016.86). The 1949 net capital loss carry-over was thus totally absorbed, producing a net capital gain included in 1950 net income, as shown in the return, in the amount of $19,251.64.

[4] As respects net capital loss carry-overs, Section 117(e)(1) provides, in effect, that a net capital loss may be carried forward to the following five years as a short-term capital loss and offset against a net capital gain for any of such years to the extent that it was not previously used.

[5] Section 122(d)(1) of the 1939 Code insofar as here relevant, provides that gains and losses from sales or exchanges of capital assets shall be taken into account without regard to the percentage limitations of Section 117(b).

ferred to in that case, as applied to the facts of this case, would require that the 1949 capital loss must be considered in computing the gain for 1950 to which the 1951 loss is to be carried back as a deduction. This holding differs materially from the taxpayer's argument that the 1949 loss must be carried forward without any reduction under Section 117(b), or, in other words, in double the amount conceded by the Government. Neither the language of Section 122 (d) (4) nor the holding in *Weinstein* or any other case would require that result.

## CONCLUSION

For the reasons stated, the petition for a writ of certiorari should be denied.

Respectfully submitted,

J. LEE RANKIN,
*Solicitor General,*

CHARLES K. RICE,
*Assistant Attorney General.*

ROBERT N. ANDERSON
DAVIS W. MORTON, JR.,
*Attorneys.*

JUNE, 1958.

## APPENDIX

Internal Revenue Code of 1939:

SEC. 23. DEDUCTIONS FROM GROSS INCOME.

In computing net income there shall be allowed as deductions:

* * * * *

(e) *Losses by Individuals.*—In the case of an individual, losses sustained during the taxable year and not compensated for by insurance or otherwise—

(1) if incurred in trade or business; or

(2) if incurred in any transaction entered into for profit, though not connected with the trade or business; or

(3) of property not connected with the trade or business, if the loss arises from fires, storms, shipwreck, or other casualty, or from theft. No loss shall be allowed as a deduction under this paragraph if at the time of the filing of the return such loss has been claimed as a deduction for estate tax purposes in the estate tax return.

* * * * *

(o) [As amended by Sec. 224(a) of the Revenue Act of 1939, c. 247, 53 Stat. 862, and Sec. 8(b) of the Individual Income Tax Act of 1944, 58 Stat. 231] *Charitable and Other Contributions.*—In the case of an individual, contributions or gifts payment of which is made within the taxable year to or for the use of:

* * * * *

(2) A corporation, trust, or community chest, fund, or foundation, created or organized in the United States or in any pos-

session thereof or under the law of the United States or of any State or Territory or of any possession of the United States, organized and operated exclusively for religious, charitable, scientific, literary, or educational purposes, * * *

* * * *

to an amount which in all of the above cases combined does not exceed 15 per centum of the taxpayer's adjusted gross income. * * *

(s) [As added by Sec. 211(a), Revenue Act of 1939, supra] *Net Operating Loss Deduction.*—For any taxable year beginning after December 31, 1939, the net operating loss deduction computed under section 122.

(26 U.S.C. 23.)

SEC. 41. GENERAL RULE.

The net income shall be computed upon the basis of the taxpayer's annual accounting period (fiscal year or calendar year, as the case may be) in accordance with the method of accounting regularly employed in keeping the books of such taxpayer; but if no such method of accounting has been so employed, or if the method employed does not clearly reflect the income, the computation shall be made in accordance with such method as in the opinion of the Commissioner does clearly reflect the income. * * *

(26 U.S.C. 41.)

SEC. 117. CAPITAL GAINS AND LOSSES.

* * * *

(b) [As amended by Sec. 150(c), Revenue Act of 1942, c. 619, 56 Stat. 798] *Percentage Taken Into Account.*—In the case of a taxpayer,

other than a corporation, only the following percentages of the gain or loss recognized upon the sale or exchange of a capital asset shall be taken into account in computing net capital gain, net capital loss, and net income:

100 per centum if the capital asset has been held for not more than 6 months;

50 percentum if the capital asset has been held for more than 6 months.

* * * *

(e) [As amended by Sec. 150(c), Revenue Act of 1942, *supra*,] *Capital Loss Carry-Over.*—

(1) *Method of computation.*—If for any taxable year beginning after December 31, 1941, the taxpayer has a net capital loss, the amount thereof shall be a short-term capital loss in each of the five succeeding taxable years to the extent that such amount exceeds the total of any net capital gains of any taxable years intervening between the taxable year in which the net capital loss arose and such succeeding taxable year. For purposes of this paragraph a net capital gain shall be computed without regard to such net capital loss or to any net capital losses arising in any such intervening taxable years.

* * * *

(26 U. S. C. 117.)

SEC. 122 [As added by Sec. 211(b), Revenue Act of 1939, *supra*, and as amended by Secs. 105(e) and 150(e), Revenue Act of 1942, supra]. NET OPERATING LOSS DEDUCTION.

(a) *Definition of Net Operating Loss.*—As used in this section, the term "net operating loss" means the excess of the deductions allowed by this chapter over the gross income, with the exceptions, additions, and limitations provided in subsection (d).

* * * * *

(d) *Exceptions, Additions, and Limitations*—The exceptions, additions, and limitations referred to in subsections (a), (b), and (c) shall be as follows:

(1) The deduction for depletion shall not exceed the amount which would be allowable if computed without reference to discovery value or to percentage depletion under section 114(b)(2),(3), or (4);

* * * * *

(4) Gains and losses from sales or exchanges of capital assets shall be taken into account without regard to the provisions of section 117(b). As so computed the amount deductible on account of such losses shall not exceed the amount includible on account of such gains.

* * * * *

(26 U.S.C. 122.)

Treasury Regulations 111, promulgated under the Internal Revenue Code of 1939:

Sec. 29.11-1. *Computation of Net Income*—Net income must be computed with respect to a fixed period. * * * It is sufficient that such items, if otherwise properly included in the computation, can be valued in terms of money. The

time as of which any item of gross income or any deduction is to be accounted for must be determined in the light of the fundamental rule that the computation shall be made in such a manner as clearly reflects the taxpayer's income. If the method of accounting regularly employed by him in keeping his books clearly reflects his income, it is to be followed with respect to the time as of which items of gross income and deductions are to be accounted for. * * * If the taxpayer does not regularly employ a method of accounting which clearly reflects his income, the computation shall be made in such manner as in the opinion of the Commissioner clearly reflects it.

Sec. 29.122-3. *Computation of Net Operating Loss in Case of a Taxpayer Other Than a Corporation.*—(a) *General.*—A net operating loss is sustained by a taxpayer other than a corporation in any taxable year if and to the extent that, for such year, there is an excess of deductions allowed by chapter 1 over gross income, both computed with the following exceptions and limitations:

> (1) The deduction for depletion shall not exceed the amount which would be allowable if computed without reference to discovery value or to percentage depletion under section 114 (b) (2), (3), or (4);
>
> * * * *

Sec. 29.122-4 [As amended by T.D. 5963, 1953-1 Cum. Bull. 197] *Computation of Net Operating Loss Carry-Overs and Net Operating Loss Carry-backs.*—(a) *In general.*—The aggregate of any net operating loss carry-overs

and any net operating loss carry-backs to a taxable year shall be the basis of the net operating loss deduction. In order to compute such deduction the taxpayer must first determine the part of any net operating losses for any preceding or succeeding taxable years which are carry-overs or carry-backs to the current taxable year.

* * * *

☆ U. S. GOVERNMENT PRINTING OFFICE: 1958 470420 1678